

Implied indemnity when acting as a director of a client company

Insights - 22/01/2018

A recent decision of the High Court in England should be carefully considered by corporate service providers in Jersey. In First Names (Jersey) Limited v IFG Group PLC [2017] EWHC 3014 (Comm) Knowles J held that there is an implied term in the contract of employment that an employee required to serve as a director of a client company, and acting in good faith, would be indemnified against costs, losses and liabilities incurred in the course of that directorship.

Although the case was heard in England, it specifically related to contracts of employment governed by Jersey law. Therefore the decision is likely to be highly persuasive if a similar issue arises before the Royal Court in Jersey and we anticipate this decision is likely to be followed to imply this term into contracts of employment here.

In summary, the facts of the case are as follows:

- Three employees of First Names Jersey were, in the course of their employment, appointed to act as directors of a client structure. Their contracts made express provision for these employees to act as directors. However, there were no express indemnities from First Names Jersey to the employees in respect of their conduct whilst acting on behalf of any client companies.
- The relevant client company entered into summary liquidation in Jersey. The liquidator issued a claim against the three directors. It was not in dispute that the directors had acted in good faith to First Names Jersey. As a result, First Names Jersey felt that it was obliged to indemnify the employees against the costs and potential damages in relation to the claim by the liquidator.
- There was a third party that may have had to reimburse First Names Jersey in relation to any expenditure in defending the claim, due to indemnities in an earlier share purchase agreement. This third party, IFG, disputed that there was an implied indemnity in the contracts of employment so as to require First Names Jersey to support their employees.

They argued that as there was no express indemnity and that there was no basis for implying an indemnity into the employment contracts, that their obligations to First Names Jersey were not engaged.

Under Jersey law, a term will only be implied into a contract where it is necessary to ensure that the contract is not rendered futile, inefficacious or absurd. Knowles J held "I respectfully regard as absurd the proposition that [an employer], having contracted to provide directors to [a client], instructed its employees to serve as directors for [that client], and arranged to charge [the client] for the work of those employee as directors, did not have an obligation to indemnify those employees in relation to the work undertaken, always assuming good faith towards [the employer]."

First Names also argued that without an implied indemnity, the employment contracts would be commercially unworkable as employees would not be prepared to act as directors for client companies. There were other factors such as the employer holding insurance to cover the client's liabilities arising from breach by the employees, which suggested that the employer accepted that it would be responsible for these breaches.

Therefore, the judge held that there was an implied term in the contracts of employment that the employer would indemnify employees, acting in good faith, as directors of client companies in respect of costs and liabilities arising out of those directorships.

The points for corporate service providers to take away from this decision are:

1. Employers can provide an express indemnity to employees within the contract of employment. The advantage of an express indemnity is that it can be tailored by the employer to define and limit the extent of indemnity. This is preferable to the general indemnity that will otherwise be implied;
2. In the absence of an express indemnity, the Royal Court is likely to imply an indemnity for employees acting as directors of client companies. It should be noted that it is possible to avoid this implied indemnity by including an express term in the contract that clearly states that there is no indemnity for employees acting as directors of client companies. Commercially, this may not be an attractive stance for employers to take as it may limit or restrict talent retention;
3. This judgment does not affect the restrictions on companies providing indemnities to their own directors or officers. This is expressly prohibited by article 77(1) of the Companies (Jersey) Law 1991. This prohibition does not apply to situations where employees are required to act as directors of client structures or companies, as the indemnity is not being provided to the employees by the client company.
4. Corporate service providers should consider their contracts of employment and review any insurance policies, including applicable directors and officers insurance, to ensure that they

are adequately protected in the event of a claim being made on either an express or implied indemnity.

Finally, there was a passing comment made by the judge in relation to corporate governance. He noted that although it is common for corporate service to provide directors to its clients, "it can have...implications for the nature of the governance that is brought to a company but here is not the place to debate that." With increased scrutiny on corporate governance in Jersey, this comment is worth bearing in mind as it is a sharp reminder to ensure that directors provide robust, independent advice to client companies, notwithstanding they remain employees of the corporate service provider.

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